

Message Text

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EXDIS FOR UNDER SECRETARY ROGERS

FOLLOWING REPEAT LONDON 18798 ACTION SECSTATE 22 NOV 76

QUOTE

C O N F I D E N T I A L LONDON 18798

EXDIS

E.O. 11652: XGDS-1

TAGS: EFIN, UK

SUBJECT: HAROLD LEVER ON IMF CREDIT AND STERLING
BALANCES

SUMMARY: HAROLD LEVER REVIEWED HIS CURRENT IDEAS ON THE
PROPOSED IMF CREDIT AND THE STERLING BALANCE PROBLEM
DURING A CALL BY SECRETARY RICHARDSON. LEVER CONTINUES
TO ARGUE THAT DEFLATIONARY MEASURES ARE UNDESIRABLE
AND THAT THE IMF SHOULD CALL FOR MONEY SUPPLY LIMITS
RATHER THAN CUTTING THE DEFICIT, BUT ACKNOWLEDGES THAT
HE PROBABLY WILL BE OVERRULED ON THIS TO SOME EXTENT.
LIKE THE PRIME MINISTER AND THE CHANCELLOR, HE
ADVOCATES AN IMF/STERLING BALANCE PACKAGE. END SUMMARY

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1. SECRETARY OF COMMERCE RICHARDSON CALLED ON HAROLD

LEVER NOVEMBER 19 ACCOMPANIED BY DCM AND EC MIN.

2. SECRETARY RICHARDSON SAID SECRETARY SIMON BELIEVES THE MEASURES THE IMF WILL REQUIRE WILL REASSURE THE MARKET. AS WE UNDERSTAND IT, LEVER, HOWEVER, IS CONCERNED WITH STERLING SELLER DECISIONS NOT RELATED TO REALITIES AND HENCE WANTS THE US AND OTHERS TO UNDERTAKE A CONTINGENT LIABILITY. HOW COULD THIS CONTINGENT LIABILITY BE DEFINED WITHOUT DENYING THE PRINCIPLE OF FREE FLOATING EXCHANGE RATES? AT WHAT POINT WOULD THE CONTINGENT LIABILITY OPERATE?

3. LEVER SAID THE ARRANGEMENT HE PROPOSES IS NOT COMPATIBLE WITH A FREE FLOAT. THE GUARANTORS WOULD NEED TO PUT A CERTAIN AMOUNT OF TRUST IN THE BRITISH GOVERNMENT, WHICH WOULD HAVE TO HAVE DISCRETION AS TO PARITY AT WHICH IT WOULD CONVERT STERLING. THE UK WOULD HAVE TO DECIDE, BUT THE OTHERS CAN TRUST THAT IT WOULD NOT BUY STERLING AT AN UNJUSTIFIABLE EXCHANGE RATE.

4. RICHARDSON SAID YOU SAY TRUST US. TO DO SO, WE NEED TO KNOW WHAT YOU ARE GOING TO DO FIRST.

5. LEVER SAID THE SAFETY NET CONCEPT IS NOT BASED ON AN ANALYSIS OF GOOD OR BAD PLANS AND ACTIONS, IT IS BASED ON A STRUCTURAL SITUATION. FOR THIS PURPOSE THERE SHOULD BE NO DISTINCTION BETWEEN THE RATIONAL AND IRRATIONAL ACTIONS OF SHEIKHS (STERLING HOLDERS). THE UK MIGHT ASK FOR THE SAFETY NET EVEN IF THERE WERE NO NEED FOR AN IMF PACKAGE.

6. RICHARDSON INSISTED THAT THE STERLING BALANCES ARE A PROBLEM BECAUSE OF BRITAIN'S ECONOMIC PROBLEMS. ANY GUARANTORS WOULD WANT TO LIMIT THEIR CONTINGENT LIABILITY BY REQUIRING ACTIONS SIMILAR TO THOSE THE IMF WOULD REQUIRE.

7. LEVER SAID YOUR SIDE WANTS ADDITIONAL LEVERAGE TOWARD DEFICIT REDUCTIONS. NO REPUTABLE OUTSIDE ECONOMIST IN THE UK SEES AN ECONOMIC CASE FOR FURTHER

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DEFLATION; THOUGH SOME SENIOR OFFICIALS DO, THE WEIGHT OF OPINION IN THE UK IS CLEARLY AGAINST. HENCE THERE IS GREAT RELUCTANCE TO FOLLOW THIS LINE. (HE NOTED IN THIS CONNECTION THAT THE INCOMES POLICY HAS BEEN SUCCESSFUL AND THE UNIONS ARE BEHAVING, WHICH HE ATTRIBUTES TO THEIR INCREASED UNDERSTANDING; THE ANTAGONISM OF LABOR TO THE BOSSES HAS CHANGED ON A MASS SCALE, AND THE REALIZATION THAT THEY ARE IN THE SAME BOAT HAS PRODUCED

A TURN AROUND THAT REPRESENTS A REAL HOPE.) HOWEVER, THE GOVERNMENT HAS TO MAKE DEFLATIONARY CONCESSIONS TO THE IMF, LARGELY BECAUSE OF THE US TREASURY'S INFLUENCE ON THE FUND AND THE RATHER RELIGIOUS IDEAS OF SECRETARY SIMON AND DR. BURNS.

8. RICHARDSON ASKED WHETHER THE REAL QUESTION IS NOT HOW TO DEAL WITH THE PUBLIC SECTOR BORROWING REQUIREMENT. LEVER SAID HE WOULD HAVE NO DIFFICULTY FINANCING THE PRESENTLY CONTEMPLATED PSBR, AND NOT AT THE PRESENT "RIDICULOUS" RATES OF INTEREST. SINCE THE OBJECT OF REDUCING THE PSBR IS TO LIMIT THE MONEY SUPPLY, THE FUND SHOULD TELL THE UKG TO LIMIT THE MONEY SUPPLY, NOT THE PSBR. THEN IF THEY CANNOT FINANCE THE PSBR WITHIN THESE LIMITS, THEY WOULD HAVE TO CUT THE PSBR, BUT HE IS CONVINCED THAT THEY CAN. LEVER INSISTED THAT THERE IS NO PROBLEM IN FINANCING THE PSBR, THOUGH HE ACKNOWLEDGED THAT DENIS HEALEY DISAGREES AND THAT ANY RESTRAINTS THE IMF WANTS SHOULD BE ON THE MONEY SUPPLY.

9. LEVER ALSO SAID A CUT IN THE PSBR IS NOT NEEDED TO MAKE ROOM FOR INDUSTRIAL EXPANSION IN A REAL RESOURCES SENSE. (SECRETARY OF STATE FOR INDUSTRY ERIC VARLEY, IN A SEPARATE CONVERSATION, TOOK THE SAME POSITION, AS DID HEALEY, BUT, AS PREVIOUSLY REPORTED, SECRETARY OF STATE FOR TRADE EDMUND DELL TOOK A CONTRARY VIEW.)

10. LEVER SAID THE PSBR OF COURSE SHOULD BE REDUCED, BUT OVER TIME TO AVOID HEAVY DEFLATIONARY MEASURES AT THE WRONG TIME. TO CORRECT THE DEFICIT IN TIMES OF HEAVY UNEMPLOYMENT WILL MAKE THE CORRECTIVE MEASURES EXTREMELY UNPOPULAR AND THE END RESULT PROBABLY WILL BE TO FORCE BRITAIN TO A SIEGE ECONOMY. EXPLAINING
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THIS, HE SAID THE LUBRICANT TO PERSUADE THE TRADE UNIONS TO ACCEPT DEFLATIONARY MEASURES WILL BE IMPORT RESTRICTIONS.

11. WE ASKED WHETHER, REGARDLESS OF THE VALIDITY OF THE FINANCING PROBLEM, A REDUCTION IN THE PSBR IS NOT NEEDED FOR REASONS OF CONFIDENCE. LEVER SAID YES, IT PROBABLY IS. ILLUSION BELIEVED ENOUGH BECOMES FACT. IN ANY CASE, HE NO DOUBT WILL BE OVERRULED AND THERE WILL BE A MODEST CONCESSION TO ILLUSION.

12. TURNING TO THE STERLING BALANCE QUESTION, LEVER

SAID THE PRIME MINISTER AGREES THE PROBLEM NEEDS TO BE DEALT WITH AND ALSO SEES POLITICAL ADVANTAGE IN DEALING

WITH IT. HE WANTS TO HANDLE THE IMF PACKAGE AND STERLING BALANCES TOGETHER TO HELP MAKE THE IMF MEASURES ACCEPTABLE. LEVER SAID THE UNITED STATES IS CONCERNED THAT THE APPROACH TO STERLING BALANCES MIGHT BE USED TO EVADE MEASURES THE FUND WOULD REQUIRE; THEREFORE IT SHOULD BE HELD OFF UNTIL LATER. THIS, HE SAID, IS NOT SO; THE TWO MUST BE HANDLED TOGETHER SINCE THE FUND CREDIT COULD LEAVE BRITAIN STILL OPEN TO RUNS ON STERLING. LEVER COMMENTED, FINALLY, ALONG THE LINES OF CHANCELLOR HEALEY, LET US AGREE ON WHAT THE IMF PACKAGE SHOULD BE, BUT HOLD OFF THE FINAL AGREEMENT AND ANNOUNCEMENT AND DEAL WITH THE NECESSARY COMMITMENT FOR THE SAFETY NET.

13. IN LATER SEPARATE CONVERSATION WITH DCM, LEVER WARNED THAT ACCEPTANCE OF IMF "DEFLATIONARY" PACKAGE WOULD PROBABLY BE ACCOMPANIED BY THREE FURTHER (IN HIS VIEW) UNDESIRABLE ELEMENTS TO MAKE IT LESS UNACCEPTABLE TO LEFT WING: SOME MOVE TO IMPORT RESTRICTIONS, FURTHER

DEFENSE CUTS AND ENLARGEMENT OF "INTERVENTIONIST" ROLE AND RESOURCES OF NEB. ARMSTRONG.
UNQUOTE KISSINGER.

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